

In brief: Sukuk (Islamic bonds) enforceable even if not Shari'a compliant (Dana Gas PJSC v Dana Gas Sukuk Ltd & Ors)

22/11/2017

Dispute Resolution analysis: Rupert Reed QC, of Serle Court Chambers, considers the decision of Leggatt J in *Dana Gas PJSC v. Dana Gas Sukuk Ltd & Ors*. Considering construction of the documents and issues of mistake, the court also rejected the argument that public policy precluded the English courts from enforcing a contract alleged to be unlawful under the laws of the UAE as a friendly foreign state. Dana Gas (DG) had conceded that the obligations at issue did not require anything unlawful to be done in the UAE, as the payment would occur in London. Thus the contract could be enforced against DG.

What are the practical implications of this case?

This decision will give reassurance in the London and Dubai sukuk markets. To date, it has been assumed that Shari'a compliance is an issue in drafting and offering sukuk, but should not arise as an issue on enforcement. Investor concerns as to the Shari'a compliance of fixed income mudarabah sukuk have been allayed by careful structuring to ensure that the mudarib's payment obligation is written under English law in a separate instrument.

However, the risks never went away. The 2007 pronouncement of Sheikh Usmani gave rise to concerns that the issuer's purchase obligations in mudarabah and other sukuk may be Shari'a non-compliant (SNC). In 2009, in *TID v Blom* [2009] EWHC 3545 (Ch), the English courts declined to enforce by summary judgment payment under a wikala said to be SNC.

In the present case, in continuing the interim injunction, albeit on the interim merits test of whether the argument of unenforceability was seriously arguable, HHJ Waksman QC had in effect *looked through* the structuring of the relevant agreements. He had found that there was a 'single purchase process', and that he should not take 'too narrow a view of what performance of the Purchase Undertaking requires or entails' by 'slicing it up'. He had found it arguable that the undertaking was unenforceable on the *Ralli Brothers* principle (*Ralli Brothers v Compania Naviera Sota y Aznar* [1920] 1 K.B. 614) (that the English court will not enforce an obligation which requires a party to do something which is unlawful in the place of performance) because part of that process insofar as performed in the UAE may have been unlawful under UAE law.

Leggatt J has now confirmed, if only after trial, that the structuring of the obligations was effective to ensure the enforceability of the issuer's payment undertaking.

What was this case about?

In 2013, Dana Gas (DG) rescheduled Islamic finance of \$D850m by way of mudarabah sukuk to be redeemed on 31 October 2017. The mudarabah agreement, written under UAE law, provided for (i) periodic distributions, and (ii) the return of a fixed redemption amount to the Trustee for the investors.

If, however, the profits and sale value of the mudarabah assets were insufficient to pay those sums, or if there were any issue as to the validity or enforceability of any instrument, then the Trustee could by notice call for DG to make payment of the redemption amount under its undertaking in then purchasing the Trustee's rights in the mudarabah assets.

That purchase undertaking was governed by English law. However, the purchase agreement by which DG would then purchase the assets was written under UAE law.

DG issued proceedings in the UAE and England seeking declarations that the sukuk were unlawful under UAE law and unenforceable in being Shari'a non-compliant. It obtained an interim injunction against performance in the Commercial Court: [2017] EWHC 1896.

Certain shareholders of DG obtained an anti-suit injunction from the UAE court prohibiting DG and the Trustee from proceeding with the English litigation. However, an investor joined the action seeking a declaration that the purchase undertaking was valid and enforceable.

After various adjournments, Leggatt J proceeded to try, as a preliminary issue, the issue of whether the purchase undertaking was valid and enforceable even if, as a matter of UAE law, all of the relevant contractual obligations were invalid and unenforceable.

What did the court decide?

Leggatt J considered DG's three arguments that the purchase undertaking was unenforceable and rejected all three of them.

First, it was said that DG's obligation, properly construed was conditional on a transfer of the assets under a valid sale agreement. The judge rejected any such conditionality because it was inconsistent with the sequencing by which the parties' entry into the sale agreement was 'following' payment under DG's undertaking. That payment was conditional only on service of an exercise notice.

Secondly, DG argued that the purchase undertaking was void for mistake, by reference to a common assumption that the mudarabah and sale agreements were valid and enforceable and that the Trustee had rights in the assets it could sell. The judge preferred an objective analysis of the parties' intentions to an inquiry as to their subjective beliefs, and noted that the gap between the assumption and reality needed to be fundamental. However, he found that the parties had contractually allocated the risk of the mudarabah and sale agreements being unlawful and enforceable, specifically in providing that these were events that could trigger DG's purchase undertaking and in avoiding any conditionality in that obligation.

Thirdly, DG, having abandoned its argument on the *Ralli Brothers* principle and Article 9(3) of the Rome 1 Regulation, submitted that it would be contrary to English public policy for the courts to enforce a contract unlawful under the laws of the UAE as a friendly foreign state, citing the principle derived from the Court of Appeal decision *Foster v Driscoll* [1929] 1 KB 470. However, since the court found no intention that the purchase undertaking should require the doing of anything in the UAE assumed to be unlawful in the UAE – because payment would occur in London – this argument also failed.

Case details

- Case name: *Dana Gas PJSC (a company incorporated under the laws of the UAE) v Dana Gas Sukuk Ltd & Ors* [2017] EWHC 2928 (Comm)
- Court: Queen's Bench Division (Commercial Court)
- Judge: Leggatt J
- Date of judgment: 17 November 2017

The views expressed by our Legal Analysis interviewees are not necessarily those of the proprietor.

FREE TRIAL